



STATE BOARD OF EQUALIZATION
STAFF LEGISLATIVE BILL ANALYSIS

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Date Amended:	04/18/01	Bill No:	AB 390
Tax:	Sales and Use	Author:	Maddox & Runner
Board Position:	Support	Related Bills:	SB 13 (McClintock)

BILL SUMMARY

This bill would repeal the provisions that provide for the imposition of a 1/4 percent state sales and use tax.

ANALYSIS

Current Law

Under existing law, Sections 6051.3 and 6201.3 of the Revenue and Taxation Code provide for the imposition of a 1/4 percent State General Fund sales and use tax rate. Sections 6051.4 and 6201.4 specify that the 1/4 percent rate imposed by these sections ceases to be operative on and after January 1 following any November 1 in which the Director of Finance certifies that:

- the amount in the Special Fund for Economic Uncertainties as of June 30 of the prior fiscal year exceeded 4 percent of General Fund revenues for that prior fiscal year, and
- the estimated amount in the Special Fund for Economic Uncertainties as of June 30 of the current fiscal year (without including any revenue derived from the 1/4 percent rate on and after January 1 of the current fiscal year) exceeds 4 percent of General Fund revenues for the current fiscal year.

Currently, a base state and local sales and use tax rate of 7 percent is imposed as noted below:

- 4 3/4 percent state tax allocated to the state's General Fund (Sections 6051 and 6201).
- 1/2 percent state tax allocated to the Local Revenue Fund which is dedicated to local governments for program realignment (Sections 6051.2 and 6201.2).
- 1/2 percent state tax allocated to the Local Public Safety Fund which is dedicated to local governments to fund public safety services (Sec. 35 of Article XIII of the California Constitution).
- 1 1/4 percent Bradley-Burns Uniform Local Sales and Use Tax which is allocated to cities and counties (Part 1.5 (commencing with Section 7200)).

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An additional local district tax ranging from 1/8 to 1 1/4 percent (referred to as Transactions and Use taxes) is imposed by special taxing jurisdictions in various counties and cities within the state (Part 1.6 (commencing with Section 7252)).

Also, as noted previously, Sections 6051.3 and 6201.3 impose a 1/4 percent state tax, which is allocated to the state's General Fund. However, the tax imposed by these sections ceased to be operative January 1, 2001 since the specified conditions have occurred.

Background

Sections 6051.3, 6051.4, 6201.3, and 6201.4 were added during the 1991 Legislative Session as part of a comprehensive package to address a \$14 billion state budget gap. At that time, the Legislature enacted SB 179 (Deddeh, Chapter 88, Statutes of 1991) and AB 2181 (Vasconcellos, Chapter 85, Statutes of 1991) to increase the sales and use tax rate by 1 1/4 percent as well as to repeal various sales and use tax exemptions.

The 1/4 percent sales tax "trigger" drew little notice through most of the 1990s as the reserve in the Special Fund for Economic Uncertainties (SFEU) fell well below the 4 percent threshold. That has changed in recent years:

In 1998-99, the year ended with a reserve of \$1.9 billion, or 3.3 percent of the General Fund revenues of \$58.2 million.

In 1999-00, the year ended with a reserve of \$7.2 billion, or 10.1 percent of the General Fund revenues of \$71.1 billion.

In 2000-01, to date, revenues are exceeding the 2000 Budget Act forecast, and the Department of Finance expects the reserve in 2000-01 to exceed 4 percent of General Fund revenues.

Note, the SFEU represents, in essence, the State's "surplus." The SFEU provides a source of funds for the general activities of the State in the event of a decline in revenues or an unanticipated increase in expenditures. This is also the residual of total resources after total expenditures and all legal reserves (such as the reserve for encumbrances).

COMMENTS

1. **Sponsor and purpose.** This bill is sponsored by the author and is intended to make permanent the 1/4 percent reduction in the state sales and use tax rate.

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2. **The April 18, 2001 amendment adds a coauthor and makes a nonsubstantive change.** Assembly Member Runner has been added as a coauthor. The bill additionally makes a nonsubstantive change.
3. **Enactment of this measure could save retailers and the Board future implementation expenses.** If this bill becomes law, the tax rate reduction would be permanent, and therefore, the Board would not be required to implement a rate change in future years when the reserve in the SFEU falls short of the 4 percent threshold. Also, retailers would not incur the associated costs with a tax rate change in future years.

Based on information in a 1990 report to the Legislature prepared by the Board to determine the impact on retailers' costs for implementing a 1/4 percent sales and use tax increase in 1989, on average, retailers with quarterly prepay accounts spent \$94.35 to reprogram their cash registers and computers, and retailers with monthly accounts and quarterly prepayment accounts spent \$19.47 for reprogramming for the 1/4 percent tax change. Adjusting these figures for an increase in the California Consumer Price Index and the increase in the number of accounts since the 1990 study, it is estimated that retailers incurred approximately \$9.3 million in comparable reprogramming costs to implement the January 1, 2001, 1/4 percent tax rate reduction. Accordingly, retailers spend at least \$9.3 million to reprogram their registers and computers each time a statewide tax rate change occurs.

However, retailers also incur other costs in implementing and administering a tax rate change. These costs include employee training, higher payroll costs associated with the resolution of customer complaints, and an increase in the cost to keep their accounting books and records and to familiarize themselves with new Board forms and tax returns to report any increase or decrease in the tax rate.

Changes in the tax rate also result in additional printing costs for the many retailers who are required to reprint menus, catalogs, invoices, and other business-related forms.

4. **Related Legislation.** Senate Bill 13 (McClintock) has also been introduced to repeal the provisions that provide for the imposition of a 1/4 percent state sales and use tax. The Board also voted to support that measure.

COST ESTIMATE

This bill would not impact the Board's current administrative costs, since the 1/4 percent statewide tax rate reduction went into effect on January 1, 2001 in accordance with the provisions of existing law. However, in future years, without the enactment of this measure, if the reserve in the Special Fund for Economic

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Uncertainties were to fall below the 4 percent threshold, the law would reinstate the 1/4 percent tax. If that were to occur, the Board would incur costs in notifying the public, revising tax returns, reprogramming, and handling the increased computational errors on returns. Potentially, these costs could be incurred on an annual basis if the SFEU reserves were to fluctuate accordingly. The costs associated with implementing a 1/4 percent statewide sales and use tax rate change are estimated to be as follows:

Implementation Costs
FY 2000-2001

\$977,000

Ongoing Costs
FY 2001-2002

\$831,800

REVENUE ESTIMATE

The provisions for the suspension of the ¼ percent rate were met during 2000-01 and the 1/4% rate has been suspended for the 2001 calendar year. Based on Department of Finance estimates, the suspension of the ¼ percent rate will result in a revenue loss to the state of \$1.1 billion.

Revenue Summary

Since the ¼ percent state sales and use tax rate has been suspended for calendar year 2001, this proposal would have no revenue effect for this year. However, this proposal would permanently repeal the ¼ percent state sales and use tax rate, which would result in an ongoing loss of approximately \$1.1 billion for each year for which the tax would not otherwise be suspended under the existing provisions of Sections 6051.4 and 6201.4.

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